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STATE ALSO FOR EAP/TC
STATE PASS USTR FOR STRATFORD AND ALTBACH, TREASURY FOR
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SUBJECT: TAIWAN ECONOMY STRUGGLES IN FIRST HALF OF 2009

11. (SBU) SUMMARY. Taiwan's economy continued to struggle through a steep slowdown during the first half of 2009. Foreign trade, domestic sales, and industrial production posted significant year-on-year declines. Inbound and outbound investment decreased sharply, inflation eased, and unemployment rose to a record high. Excess liquidity contributed to strong stock market rally. Taiwan's official GDP forecast for 2009 is -4.25%, with most private forecasts predicting GDP declines in the range of -5% to -7%. END SUMMARY.

12. (SBU) Trade and Industrial Production Begin to Show Signs of Recovery: After suffering steep year-on-year (yoy) plunges in the second half of 2008 and Q1 of 2009, trade and industrial production followed the Q2 cyclical upward trend that has also been apparent in past years. Taiwan's Q2 exports rose 18% from Q1 to US\$48 billion, while its Q2 imports increased 27.6% to US\$40.9 billion. Q2 domestic sales (i.e., wholesale plus retail sales) also increased 6.6% from Q1 to NT\$3 trillion (US\$91 billion). Meanwhile, manufacturing production in Q2 grew by 31% from Q1.

13. (SBU) Double-digit Year-on-year Fall in Foreign Trade: Taiwan's foreign trade in Q2 continued to post negative year-on-year (yoy) growth, including a 32% drop in exports and a 38% fall in imports, a slight improvement over the Q1 figures of -36.7% and -47.2%, respectively. Q2 exports to China (including Hong Kong), Taiwan's largest export destination, fell by 31% yoy, more than the declines of 30% and 25% in exports to the U.S. and Japan, respectively. Taiwan's Q2 exports to ASEAN and the EU also dropped by 29.4% and 36.8%, respectively. These five markets account for 85% of Taiwan's total exports. Q2 shipments from Japan, Taiwan's largest import source, fell by 33% yoy, less than the respective declines of 37% and 43% in imports from China and the U.S. Taiwan's Q2 imports from ASEAN and EU also dropped by 29.5% and 35.5%, respectively. These five sources supplied two-thirds of Taiwan's total imports.

14. (SBU) Investment Drops: Q2 imports of capital goods, an important investment indicator, fell by 40% year-on-year to US\$5.5 billion. Approved inbound direct investment in Q2 plunged by 71% year-on-year to US\$739 million, the lowest level in the past five years. Approved outbound direct investment in Q2 dropped by 48%, including a fall of 55% in investment bound for the PRC.

15. (SBU) Excess Liquidity Contributes to Stock Market Rally: Excess liquidity has been a reflection of interest rates at about 1% in Taiwan's call loan inter-bank market, as well as relatively high money supply growth. M1B (i.e., currency held by the public plus deposit money) in June grew by 17% year-on-year, the highest rate in

the past five years. Excess liquidity helped contribute to a 40% rise in Taiwan's stock index during the first half of the year, and an additional 11% increase through July 29.

¶6. (SBU) Record High Unemployment Rate: Prices have been stable, with the inflation rate at -0.43% in the first half of the year. The unemployment rate, however, rose to a record high of 5.91% in June. The unemployment rate is expected to continue to rise as new graduates enter the labor market over the summer.

¶7. (SBU) Taiwan sells relatively less to the PRC: According to the PRC trade data for the first five months of 2009, imports from Taiwan posted a 39% year-on-year (yoy) decline, more than declines of 28% from Japan, 25% from South Korea, and 17% from the U.S. As a result, Taiwan dropped from third to fourth as a source of PRC imports during the first five months of the year.

WANG